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IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS

In re:	
KEITH CHARLES MUNK,	**CASE NO. 86-40195-7**
MARY HELEN MUNK,	**CHAPTER 7**
DEBTORS.	

MEMORANDUM OF DECISION

This matter is before the Court on the debtors' motion to hold the Farm Service Agency ("FSA") in contempt for violating the discharge injunction imposed by 11 U.S.C.A. §525. The debtors appear by counsel Phillip L. Turner. The FSA appears by counsel Tanya Sue Wilson. The Court has reviewed the relevant materials and is now ready to rule.

In 1987, the debtors received a chapter 7 bankruptcy discharge of a debt to the Farmers Home Administration ("FmHA"), a predecessor of the FSA. In 1998, they applied for a direct operating loan from the FSA. Because of the discharge of the FmHA debt, the FSA denied the debtors application, as its regulations required it to do. The debtors have now asked the Court to hold the FSA in contempt for violating the anti-discrimination provisions of 11 U.S.C.A. §525.

Section 525(a) of the Bankruptcy Code provides in pertinent part that:

> [A] governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, [or] discriminate with respect to such a grant against, . . . a person that is or has been a debtor under this title . . . solely because such . . . debtor is or has been a debtor under this title . . . , has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title. . . .

Most of the courts, including all the circuit courts, considering the question have concluded that this provision does not prevent a governmental unit from refusing to extend new credit to a potential borrower because he or she had previously obtained a bankruptcy discharge. *See, e.g., Toth v. Michigan State Housing Development Authority*, 136 F.3d 477 (6th Cir. 1998); *Goldrich v. New York State Higher Education Servs. Corp.*, 771 F.2d 28, 29-31 (2d Cir. 1985) (decided before subsection (c) was added to §525); *United States v. Cleasby*, 139 B.R. 897 (W.D. Wis. 1992); *see also Watts v. Pennsylvania Housing Fin. Co.*, 876 F.2d 1090, 1093-94 (3d Cir. 1989) (state loan program that paid certain homeowners' mortgage obligation to prevent threatened foreclosure suspended payments while automatic stay prevented foreclosure; Third Circuit declared loan is not "similar grant" to those expressed in §525). *But see Richardson v. Pennsylvania Higher Education Assistance Agency (In re Richardson)*, 15 B.R. 925 (Bankr. E.D. Pa. 1981) (state regulation would violate §525 (before subsection (c) was added) by requiring residents who had discharged previous student loans and were applying for new ones to appeal initial denial of new loans when residents with no prior loans would automatically be approved for loans), *vacated* 27 B.R. 560, 564 (E.D. Pa. 1982) (regulation could be applied without violating Bankruptcy Code because §525 did not bar state agency from making reasonable inquiry into applicant's future financial responsibility, which could apparently include consideration of applicant's previous bankruptcy); *Rose v. Connecticut Housing Fin. Agency (In re Rose)*, 23 B.R. 662, 665-67 (Bankr. D. Conn. 1982) (§525 prohibits exemption of bankrupts from mortgage financing program solely because of their bankruptcies; however, former bankrupt failed to establish mortgage denial was solely because of his bankruptcy). This Court agrees with the majority of courts that §525(a) does not apply to a governmental unit's decision whether to extend credit to a

person who has received a bankruptcy discharge. At least in the context of governmental units, a "license, permit, charter, or franchise," in this Court's view, is a right or privilege that only the government can bestow to do something that is typically illegal or punishable if done without the government's permission. *See Black's Law Dictionary* at 829 ("license"), 1026 ("permit"), 214 ("charter"), & 592 ("franchise") (5th ed. 1979). A loan, by contrast, can be obtained from other sources and merely gives the borrower money to spend; it does not give the borrower permission to do something that would be illegal but for the loan. Furthermore, in ordinary English usage, a license, permit, charter, or franchise can be said to be denied, revoked, suspended, or renewed, but a loan cannot be said to be revoked or suspended, except perhaps in the limited circumstance of a loan approved but not yet disbursed by the lender. Revocation and suspension both indicate that a thing granted in the past has been nullified or rendered no longer effective, actions that make little or no sense if said of a loan that has already been disbursed to the borrower.

The debtors suggest that the addition of subsection (c) to §525 indicates that Congress intended to prohibit governmental units from denying an application for any kind of new credit because of the applicant's prior bankruptcy discharge. Subsection (c) provides:

> (1) A governmental unit that operates a student grant or loan program and a person engaged in a business that includes the making of loans guaranteed or insured under a student loan program may not deny a grant, loan, loan guarantee, or loan insurance to a person that is or has been a debtor under this title . . . , or another person with whom the debtor . . . has been associated, because the debtor . . . is or has been a debtor under this title . . . , has been insolvent before the commencement of a case under this title or during the pendency of the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in a case under this title . . . .

> (2) In this section, "student loan program" means the program operated under part B, D, or E of title IV of this Higher Education Act of 1965 or a similar program operated under State or local law.

This provision was added to the Code by the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, §313, 1994 U.S.C.C.A.N. (108 Stat.) 4106, 4140-41, and was intended to overrule the Second Circuit's decision in *Goldrich*, 771 F.2d 28 (cited above), H.R. Rep. No. 103-835, at 58, *reprinted in* 1994 U.S.C.C.A.N. 3340, 3367. The Court cannot agree that this amendment shows Congress's intent that §525 should apply to all types of loans. If it had such an intent, Congress would not have specifically limited the new provision to student loans, and would probably have added a phrase covering loans to subsection (a) rather than creating a new subsection. The amendment Congress did pass more likely indicates instead that it agreed with the courts that had held subsection (a) did not apply to loans, and that it wanted §525 to cover student loans but not other kinds of loans. Significantly, many, if not all, the student loan programs identified in subsection (c) do not base eligibility on an applicant's present creditworthiness or ability to pay (except to the extent that they typically limit the total amount one person may owe in outstanding student loans), but instead rely on the assumption the education made possible by the student loan will increase the applicant's earning potential and future ability to repay the loan. The Court is aware of no other loan program that works this way. Ordinarily, loans are made based on a present ability to repay or at least an ability to repay that the loan itself is expected to create immediately or relatively soon, rather than at some indeterminate future date. This distinction may explain why Congress chose to subject student loans but no other loans to §525.

The debtors also rely on the Fifth Circuit's decision in *Exquisito Services, Inc., v. United States (In re Exquisito Services, Inc.)*, 823 F.2d 151 (5th Cir. 1987) (2 to 1 decision). That case

involved a program operated by the Small Business Administration (SBA) for socially and economically disadvantaged small businesses. *Id*. at 152. Under the program, appropriate government contracts would be given to the SBA rather than awarded through competitive bidding, and the SBA would then subcontract the work to businesses it had previously approved. *Id*. Exquisito Services, Inc., had such a subcontract to provide food services at an Air Force base for a primary term of one year and options for the Air Force to continue the contract for two one-year periods. *Id*. When Exquisito filed a chapter 11 bankruptcy, continuing to operate its business as a debtor-in-possession, the Air Force told the company the extension options would not be exercised because of the bankruptcy. *Id*. Before the bankruptcy court, Exquisito claimed the Air Force decision violated §525(a), and that court agreed. *Id*. On appeal, the district court affirmed. *Id*. The Fifth Circuit found the contract arrangement constituted a "franchise," saying:

> As part of the . . . program, the SBA contracted with the Air Force to provide services. The SBA then determined that Exquisito would have the exclusive right to perform them according to the terms and for the length of that contract. During the life of the contract the SBA would assist Exquisito. The program is, therefore, essentially a franchise as defined in Black's Law Dictionary (5th ed. 1979). As such, it is included within the scope of 11 U.S.C. §525(a) and discrimination against Exquisito solely because of filing under Chapter 11 is prohibited.

Id. at 154. The Circuit did not specify which portion of Black's lengthy definition of "franchise" it was relying on to reach this conclusion. It appears to this Court, however, that the following portions were probably seen as relevant:

> **Franchise**. A special privilege conferred by government on individual or corporation, and which does not belong to citizens of country generally of common right. [Citation omitted.]
> . . . .
> . . . .

> . . . . More broadly stated, a "franchise" has evolved into an elaborate agreemenet under which the franchisee undertakes to conduct a business or sell a product or service in accordance with methods and procedures prescribed by the franchisor, and the franchisor undertakes to assist the franchisee through advertising, promotion, and other advisory services. [Citation omitted.]

Black's Law Dictionary 592 (5th ed. 1979).

This Court believes *Exquisito* is distinguishable from the present matter for several reasons. A contract under which the debtors would only be required to repay money is very different from one under which they would be required to provide services to a third party. Unlike a subcontract to perform a contract the SBA had obtained from another agency, a loan of money does not seem to be a "special privilege" the FSA would grant to anyone. Once it had the Air Force contract, the SBA had to confer it on someone so the Air Force would receive the services it needed. The right to perform that contract was one only the SBA could grant, just as a license, permit, charter, or franchise granted by a governmental unit is a right available only from that unit. Many private as well as governmental lenders of various types exist, and the debtors could at least have tried to obtain a loan from any of them. To this Court, the "grants" listed in §525(a) concern rights or privileges available only from the government, not from private businesses.

In short, the Court does not find any of the debtors' arguments convincing, and concludes that the FSA did not violate §525 by denying the debtors' loan application because of their discharge of a debt owed to the FSA's predecessor. Consequently, the Court need not consider the FSA's arguments that other circumstances preclude the Court from granting the relief the debtors seek.

The foregoing constitutes Findings of Fact and Conclusions of Law under Rule 7052 of the Federal Rules of Bankruptcy Procedure and Rule 52(a) of the Federal Rules of Civil Procedure. A judgment based on this ruling will be entered on a separate document as required by FRBP 9021 and FRCP 58.

Dated at Topeka, Kansas, this ____ day of September, 1999.

_____
JAMES A. PUSATERI
CHIEF BANKRUPTCY JUDGE

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JUDGMENT ON DECISION

This matter was before the Court on the debtors' motion to hold the Farm Service Agency ("FSA") in contempt for violating the discharge injunction imposed by 11 U.S.C.A. §525. The debtors appeared by counsel Phillip L. Turner. The FSA appeared by counsel Tanya Sue Wilson. The Court reviewed the relevant materials and has now issued its Memorandum of Decision resolving the parties' dispute.

For the reasons stated in that Memorandum, judgment is hereby entered denying the debtors' motion.

IT IS SO ORDERED.

Dated at Topeka, Kansas, this _____ day of September, 1999.

JAMES A. PUSATERI
CHIEF BANKRUPTCY JUDGE